

**CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM
STATEMENT OF INVESTMENT POLICY**

**FOR
ACTIVE DOMESTIC EQUITIES – EXTERNALLY MANAGED**

February 14, 2005

This Policy is effective immediately upon adoption and supersedes all previous externally managed active domestic equities policies.

I. PURPOSE

This document sets forth the investment policy (“the Policy”) for the Externally Managed Active Domestic Equities Program (“the Program”). The design of this Policy ensures that investors, managers, consultants, or other participants selected by the California Public Employees’ Retirement System (“the System”) take prudent and careful action while managing the Program. Additionally, use of this Policy provides assurance that there is sufficient flexibility in controlling investment risks and returns associated with this segment of the U.S. capital markets.

II. STRATEGIC OBJECTIVE

Capturing returns of domestic equity markets while diversifying risk is the strategic objective for the Program.

The Program shall be managed to accomplish the following:

- A. Diversify the System’s overall Equity Program by complementing the Passive Domestic Equity Program;
- B. Enhance the expected return of the System’s investment program;
- C. Hedge against active member (pre-retirement) liabilities; and
- D. Consider solely the interests of the System’s participants and their beneficiaries in accordance with California State Law.

III. RESPONSIBILITIES AND DELEGATIONS

- A. The **System’s Investment Committee** (“the Investment Committee”) is responsible for approving and amending the Policy. The Committee delegates the responsibility for administering the

Program to the Investment Staff through the Delegation of Authority (Delegation Nos. 89-13 and 95-50).

B. The **System's Investment Staff's** ("the Staff") duties include, but are not limited to, the following:

1. Developing and recommending the Policy to the Investment Committee.
2. Developing and maintaining a procedures manual, subject to periodic review and updating, that outlines Staff operational procedures used in implementing this Policy.
3. Implementing and adhering to the Policy.
4. Recommending action concerning outside money management firm(s) ("Managers") retained under contract to implement the Program. The Staff shall make recommendations in accordance with the Manager Monitoring - Externally Managed Policy, regarding changes in the Manager's contractual guidelines, and any other aspect Staff considers pertinent.
5. Reporting to the Investment Committee, as needed, about the performance of the Program. The Staff shall monitor the implementation of, and compliance with, the Policy. The Staff shall report concerns, problems, material changes, and all violations of Guidelines and Policies immediately and in writing to the Investment Committee. Such reports to the Investment Committee shall include explanations of the violations and appropriate recommendations for corrective action.

C. **Managers** are responsible for all aspects of portfolio management as set forth in Manager's contract with the System and shall fulfill the following duties:

1. Communicate with the System's Staff, as needed, regarding investment strategies and results. The Investment Committee and Staff expect Managers to monitor, analyze, and evaluate performance relative to the agreed-upon benchmark.
2. Cooperate fully with the System's Staff, Custodian, and General Pension Consultant concerning requests for information.

- D. The **General Pension Consultant** is responsible for monitoring and evaluating each Manager's performance relative to the benchmark and Policy. The General Pension Consultant shall report to the Investment Committee on a quarterly basis, in accordance with its contract.

IV. PERFORMANCE OBJECTIVE

The Active Domestic Equity Program encompasses the Externally Managed Domestic Equity Strategies and the Internally Managed Dynamic Completion Fund (the DCF). The Program is expected to outperform the custom Wilshire 2500 Index. Within the Program, Managers or portfolios or both are expected to achieve performance objectives as stated in their Investment Management Guidelines.

V. INVESTMENT APPROACHES AND PARAMETERS

A. Approaches

1. Active domestic equity strategies shall be identified based upon their ability to add value above a style-specific benchmark on a risk-adjusted basis. The DCF will be used to attempt to neutralize any style bias.
2. The Program shall be implemented through the retention of external managers. External manager selection shall occur in accordance with Section V.B. of this Policy.
3. The System shall continually review the viability of the program, conducting a formal review at least every five (5) years.

B. External Manager Selection

1. The System shall retain managers that have recognized expertise in the analysis and selection of U.S. equity securities or approved derivatives. The selected managers shall be registered, or appropriately exempt from registration, with the Securities and Exchange Commission.
2. The System shall select the managers in accordance with the Contract and Procurement Policy.

C. Investment Parameters

The Managers shall operate under a set of specific guidelines that outlines their investment philosophies and approaches, representative portfolio characteristics, permissible and restricted securities and procedures, benchmark, and performance objectives.

Implementation of this Program shall comply at all times with the System's investment policies including, but not limited to, the following parameters:

1. Statement of Investment Policy for Derivatives - External Money Managers;
2. Proxy Voting Policies;
3. Manager Monitoring - Externally Managed Policy; and
4. Manager-specific Investment Management Guidelines.

VI. BENCHMARKS

The System shall measure individual Managers against appropriate style benchmarks. The aggregate of the active managers and the Dynamic Completion Fund shall be measured against the System's custom Wilshire 2500 Index.

VII. GENERAL

- A. Terms in this policy are defined in a master glossary of terms.
- B. Investors, managers, consultants, or other participants selected by the System shall base all calculations and computations on market value as recorded by the System's Custodian.

VIII. GLOSSARY OF TERMS

The Equities Glossary of Terms is referenced in the System's Master Glossary of Terms.